

Michigan State University, in a unique deal that has the student loan industry buzzing, will be back in the FFEL business this Fall after the school's decade-long sojourn in direct lending.

By **RICHARD D. R. HOFFMANN**

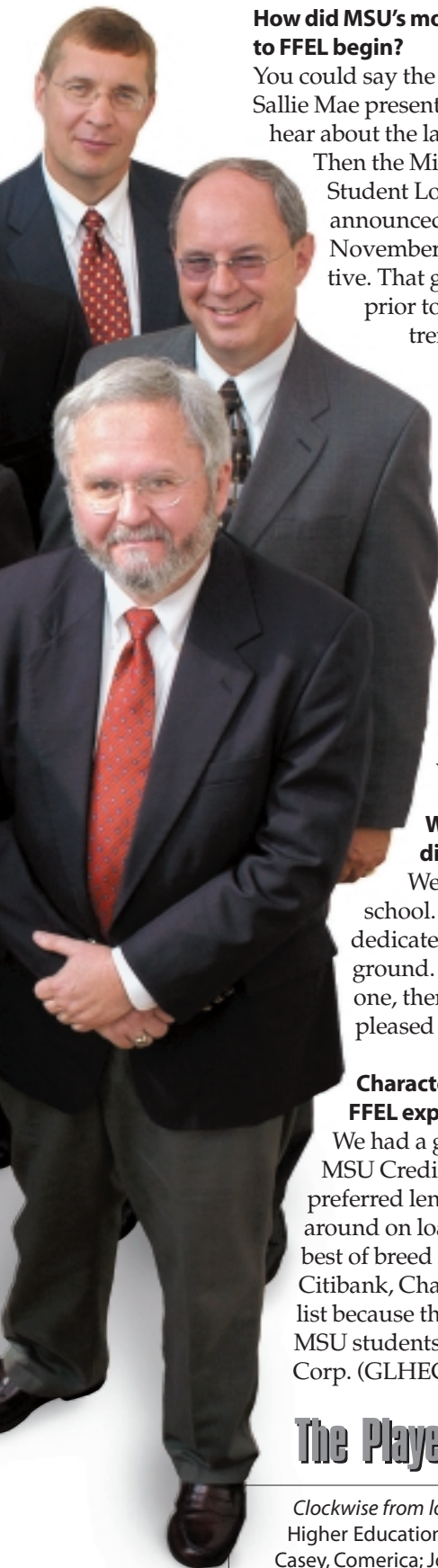
Together Again



The second-largest lender of federal Ford Direct Student Loans, MSU will begin the fall 2003 semester as a partner of the Michigan Students First Coalition (MSFC) for undergraduate student and parent loans. The school has also adopted the "school-as-lender" model for graduate and professional student loans.

The cast of characters includes three banks—Comerica, National City and Standard Federal. Each will contractually share in MSU's undergraduate volume. MHESLA the secondary market-maker that hammered the deal together, and guarantor/servicer Great Lakes Higher Education bring additional services to a unique team.

Rick Shipman, MSU's director of financial aid, is the deal's principal architect. He's a 28-year full-time MSU employee, with undergraduate and graduate degrees at the university. During the past 26 of those years Shipman has worked every conceivable job in the financial aid department, until being appointed as its director two years ago. His recent discussion with The Greentree Gazette's editor Richard Hoffmann well displays Shipman's experience and focused perspective.



How did MSU's move from direct lending back to FFEL begin?

You could say the move began when we went to a Sallie Mae presentation in Chicago last year to hear about the latest things in the FFEL industry.

Then the Michigan Higher Education Student Loan Authority (MHESLA) announced "Michigan Students First" in November 2002, and it looked very attractive. That got us moving. About two years prior to that we began not to like the trends we were seeing develop in direct lending.

What direct lending factors concerned you in particular?

There were two. We were concerned about federal support for the direct lending program. It's been small over the last several years. We wanted to be part of a dynamic student loan program, one that would grow technically to meet the demands of students – the way direct lending was when we started.

When did MSU join direct lending?

We joined in 1994 as a "year two" school. We were not in a position to dedicate a lot of resources to get it off the ground. So we observed during year one, then left FFEL and were very pleased with our choice.

Characterize your previous FFEL experience.

We had a good program back then. The MSU Credit Union was at the top of our preferred lender list, with a 24-hour turnaround on loan funds. That definitely was best of breed in FFEL at the time. Otherwise, Citibank, Chase and Bank One were on our list because they were the home banks of most MSU students. Great Lakes Higher Education Corp. (GLHEC) was the originator, guarantor

The Players

Clockwise from lower left: Patricia Scott, Michigan Higher Education Student Loan Authority; Marianne Casey, Comerica; John Nickless, Comerica; Michael Foster, Standard Federal; Gary Sole, National City; Bruce Ter Haar, Great Lakes Higher Education Corp.; David Harmon, Great Lakes Higher Education Corp.; Rick Shipman, Michigan State University (center)

Top 100 direct loan schools, 2001-02

	Rank	\$ loaned
Ohio State University	1	\$173,478,406
Michigan State University	2	\$163,330,320
University of Minnesota, Twin Cities	3	\$153,757,308
University of Florida	4	\$148,556,150
University of Michigan, Ann Arbor	5	\$134,247,511

Source: U.S. Dept of Education

and servicer. However, in those days they could not match the streamlined approach of direct lending, which we were told would replace FFEL. We wanted to get involved early and help shape the direct loan program.

Over time, things changed in direct lending?

The delivery processes in direct lending largely stayed the same, with a "one-size-fits-all" approach. It did not seem to be a stable-enough environment. U.S. Department of Education (ED) officials said publicly that they did not want to do any marketing to increase the program's market share. The current administration wants to make the program's funding discretionary. We believe that means it will be picked away at. Unless the feds put dollars and resources behind direct lending and added every new technology that's out there, I was afraid that it would wither.

What FFEL factors were involved?

We saw in FFEL a customizable program for students and institutions, right down to e-signatures for online promissory notes. FFEL seemed positioned to offer more benefits to institutions and to students. From our vantage point, it beat direct lending hands down. We could no longer in good conscience say that direct lending was better.

What was your first step in the move?

We sent 14 vendors a request for information (RFI). We gave them our volume, our default rates over the last eight years, our costs of attendance for various student categories and asked what they could do for us in a FFEL solution.

How did they respond to your RFI?

Well, we were prepared not to be surprised, but we were. They surpassed the benefits of direct lending with the borrower benefits they offered, with their willingness to help and to customize processes and user interfaces. The biggest surprise was that every one of the 14 vendors offered those things.

Who were the vendors that finally responded?

I don't remember them all, but we selected five to make individual presentations, including Sallie Mae, Nelnet, MHESLA, Key Bank and Northstar. We had made it clear we were interested in doing business with folks who had a presence in our region, reasonable market share, a reference-able reputation and an attractive set of benefits. Then we put out an RFP to them in April 2003.

Who won the bid?

A group called the Michigan Student First Coalition. MHESLA pulled together three banks, with itself as the secondary market, and GLHEC as the originator/guarantor and servicer. It was pretty sophisticated. We preferred not to deal with more than one lender, so they figured out a way for that to happen. Our preferred lender list now is one bank, Comerica, with two other banks participating in the background. The contract runs for three years.

What were some specifics of the RFP?

Our requirements were only two pages long. Page one included system conversion, user interface, loan origination, school-as-lender and borrower benefits. Page two was for options. Included was the provision for MSU to offer opportunity loans, on a professional judgment basis, to any student, including foreign nationals, with no cosigner or credit check required. Also included was an enhanced PLUS deferment to allow parents to waive payments while their students are in school. We requested a specific loan purchase premium rate for school-as-lender FFEL loans. We wanted either a fixed premium rate or a tiered option that was better than the fixed rate. We wanted borrower benefits at least as good as direct lending.

Any other RFP specifics?

We wanted a good return on the school-as-lender model. A group of our own financial analysts ran the numbers within the proposed borrower benefits and school-as-lender arrangements, and they checked out. And we wanted one lender and one servicer for everything.



“I hope we can serve other Michigan schools and students. But then again, we've always served both direct and FFEL schools with programs like paying the National Student Clearinghouse fees on loans for all Michigan students.”

Patricia Scott
Executive director, MHESLA

“Of our three campuses, two are running direct loan systems at Champaign-Urbana and in Chicago. FFEL is running in Springfield. I don't think it will be much of a technical problem for Michigan State to switch over.”



Judith Flink
*Director of student financial services,
University of Illinois, Chicago*

“MSU's move is an attention-getter, no doubt. Certainly a school that size, which once thought direct lending was good and now thinks FFEL is, should stimulate some of the bigger schools to think twice.”



Dick Willey
President & CEO, AES/PHEAA

“We're hopeful that we'll be able to do business with MSU in the future. We were one of many that worked with them, and we are very excited that they are coming into the FFEL community.”



David Bottegal
*Executive vice president of marketing
and sales, Nelnet*

What borrower benefits did MSU students wind up with?

Students and parents get a full rebate of their loan origination fee, as compared to the current 1.5% rebate in direct lending. After 36 months of on-time payments, the borrower's interest rate drops to 0%! There is a 0.25% interest rate reduction when repayment begins for borrowers who sign up for automatic payment from their bank account. Direct lending doesn't offer similar terms. Based on current interest rates, these terms could save MSU borrowers \$140 for every \$1,000 borrowed. The average MSU senior, who relies on Stafford and PLUS loans, graduates owing almost \$19,000. That student will save over \$2,600.

What made you choose the coalition?

The best way to get what we needed turned out to be partnering. Any one of them could have funded it alone, but not all could have given us the entire solution. This way, they can stay in their comfort zones. It's my understanding that this approach is unique, but I think we'll see more of it in the future. It provides the best opportunity for lenders to participate in what may become a statewide Michigan undertaking.

Have you changed your private alternative loan offerings?

No changes yet. We have a task force looking into it. If we can come up with improvements, we will. For now our current preferred alternative loan lenders include Sallie Mae Signature loans, Citibank's CitiAssist and the MHESLA MI-loan. We also accept anything else a student brings to us.

How about special services for MSU?

While all three banks participate in undergraduate loans, Comerica is the lead or "single-point of contact" bank for MSU. National City and Standard Federal, will help fund the loan portfolio and share in profits. Meanwhile, National City will provide the opportunity loans for MSU students. Standard Federal is advancing us a \$60 million line of credit to fund our school-as-lender operations.



“Other servicers have been moving into Michigan as lenders. Our coalition came together in part to assert our role in the state as lenders with a strong retail presence.

Marianne Casey
*Manager of educational lending,
Comerica Bank*

Why take on the school-as-lender model amid all the change?

Why not? We have large graduate and professional enrollments here, and we have the opportunity to provide absolutely the best benefits along with a more customized level of service. Medical students, for example, have a very demanding curriculum with little time to spend making loan decisions. The buck stops here if MSU is their lender.

Was the Board of Trustees supportive?

I thought their approval would be the hardest part, but they wound up in unanimous agreement. They saw it as a low-risk, no-cost course of action that's good for the institution, for students and parents, and for the Michigan economy. They liked that fact that this is a coalition of Michigan-based lenders. Supporting the state is good public service.

How will you administer the school-as-lender piece?

We'll bid that out independently each year. We'll realize revenue when we sell the loans on the secondary market, and it will be used exclusively to enhance our institutional financial aid programs, which now total about \$35 million per year.

Why not use the revenues to support operations?

Though the money we expect would very nicely cover the financial aid budget, effectively making us self-

Top FFEL schools, 2001–02

	Rank	# of loans	\$ loaned
University of Phoenix	1	193,103	\$948,295,297
Nova Southeastern University	2	54,515	\$368,719,682
New York University	3	41,363	\$311,688,999
Pennsylvania State University	4	72,226	\$302,175,454
University of Southern California	5	26,931	\$211,430,106
University of Texas, Austin	6	38,099	\$195,284,329
Temple University	7	36,081	\$192,418,694
DeVry University	8	48,224	\$185,567,828
• Michigan State University (9)		46,787	\$163,330,320
University of Pittsburgh	9	26,789	\$152,161,236
University of California, Los Angeles	10	28,580	\$148,035,058

Based on US Department of Education data

• Number two in direct loan dollar volume during 2001–02, MSU's volume would have placed it ninth among FFEL schools.

supporting. However, we're not using that approach here. There's an ethical issue. We could be accused of raising student borrowing so that the school will benefit.

What are the technical hurdles in making the switch?

Great Lakes is doing the bulk of the work to convert us, and they are absolutely fantastic. They are ahead of where we need to be, leading us to the next step. Three weeks after we decided to go ahead, we already had parents in the PLUS loan process! Of course, my office will be busy behind the scenes for perhaps a year. We want to be a partner with all the players in improving services.



“This is a terrific vote of confidence. It will send a message to all the direct lending schools that may be considering a change. A successful technical transfer to FFEL will also send the message that what many think is daunting is actually very do-able.

Dave Harmon

*Vice president of marketing,
Great Lakes*

Do you anticipate a greater workload for your staff?

No. Right now we have about 44 full-time staff members, down from 65 in 1995. Yet we're servicing more students, more quickly, and processing more dollars than we did with a larger staff.

After the conversion, we think there will be a zero-sum change. The entry of borrower data and the reconciliation of accounts is very labor-intensive under direct lending, and it's not required under FFEL. We'll still do data exchange, but we anticipate no overall increase in workload.

What do you fear about the changeover to FFEL?

I have no fear about successful implementation. My only fear is that early on we will be hard-pressed to spend sufficient time with our students and families. We didn't anticipate the number of calls and foot traffic we've seen. But we'll balance the work. Summertime just won't be as relaxed as usual this year.

Will your direct lending experience prove useful?

With our large student population, we've seen some of everything in the loan business. We can provide a broad perspective for our partners in order to help them fine-tune their services and offerings. Our experience should also prove helpful as FFEL moves to Common Origination and Disbursement (COD) and the

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XML format scheduled for 2004. One of our staff people here, a recognized leader in direct lending for COD, will shift her attention to the FFEL focus and share her expertise.

How do you feel about leaving direct lending?

We've gotten to know a number of people really well, so there is a certain sadness. But things are moving very fast, and we've already gone through the seven stages of grief. We certainly enjoyed being a part of it, and we had a lot of input shaping the details when it was clearly the best. But it's now second-best, and we're happy to be re-entering what we now see as the best program for our students.

Do you have an opinion regarding direct lending's future?

With the competitive nature of the student loan industry, direct lending may not have much of a future without top-level federal support to grow the program, to remain competitive and meet the new demands of borrowers. I don't see the federal government increasing its support.

Has there been feedback from ED?

No. I contacted the direct loan people at ED, asking if they wanted to submit something to consider in our review. They had nothing to submit. I was disappointed, really, that they didn't have a list of benefits comparing themselves to FFEL. But when we saw the FFEL benefits, it was, why bother? There's no reason they can't offer more than the 0.25 percent interest-rate reduction for ACH. If the FFEL vendors are offering more, why can't direct lending? And why are they charging the going interest rate, when FFEL is beating it?

What have other direct lending schools said to you?

Before Christmas last year, we called the National Direct Student Loan Coalition (NDSLCL) to tell them about our RFI and RFP. We also contacted all the financial aid directors in the Big 10 and the 15 four-year public schools in the state of Michigan, all but one of which, Wayne State, are



“What put our coalition ahead of the others competing for MSU's loan business was our agreement to provide a single point of contact through a lead Michigan bank. All of the dollars remain within the state borders. That was something no one else could offer.”

Mike Foster

*Assistant vice president,
Standard Federal Bank*

direct lending institutions. I also notified them once we made our decision. We've received nothing but positive feedback from all of them. NDSLCL wanted to know the details. The general response in a nutshell has been, “More power to you!”

Do you think other large schools will follow your lead?

Yes, I do. They are all seeing the same world we are. I know that many are actively considering a return to FFEL. The Michigan Student First Coalition is offering the same deal to any school in Michigan. It's probably too late for anyone else to switch for fall 2003, but we'll see a shift for fall 2004. ■



“My guess is that other schools will be looking at this. My hope is it will last indefinitely. It gives us a leg up, but not forever if we don't perform.”

Gregory Stringer

Senior vice president, National City Bank